

No. 16330 ✓

United States
Court of Appeals
for the Ninth Circuit

CHARLES E. HOPPE, Trustee of the Estate of
Los Gatos Lumber Products, Inc., Bankrupt,
Appellant,

vs.

EMMET L. RITTENHOUSE,
Appellee.

Transcript of Record

Appeal from the United States District Court for the
Northern District of California,
Southern Division.

FILED

JUN - 3 1959

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INDEX

[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

	PAGE
Appellant's Concise Statement of Points Urged on Appeal	80
Attorneys, Names and Addresses of	1
Certificate of Clerk to Record on Appeal	77
Findings of Fact and Conclusions of Law	13
Hearing on Order to Show Cause	30
Witnesses:	
Gammill, Paul, Jr.	
—direct	33
—cross	41, 73
—redirect	76
Morton, Carl	
—direct	46, 55
—cross	61
—redirect	72
Notice of Appeal	29
Notice of Hearing	28
Order of Adjudication	8
Order Affirming Referee	29
Order Allowing Secured Claim	18

INDEX	PAGE
Order of Reference	7
Order to Show Cause	9
Petition by Creditors	3
Referee's Certificate on Petition for Review of Findings of Fact and Conclusions of Law and Order Allowing Secured Claim	19
Statement of Affairs	6
Trustee's Objection to Proof of Secured Claim of Emmet L. Rittenhouse	10

NAMES AND ADDRESSES OF ATTORNEYS

SHAPRO & ROTHSCHILD,
DANIEL ARONSON, JR.,

P.O. Box 508,
Burlingame, California,

For Appellant.

GEORGE P. STEPOVICH,
131 W. Main Street,
Los Gatos, California,

For Bankrupt.

EMMETT L. RITTENHOUSE,
Rittenhouse Building,
Santa Cruz, California,

For Claimant.

In the Southern Division of the United States
District Court for the Northern District of
California.

No. 47996—In Bankruptcy

In the Matter of:

LOS GATOS LUMBER PRODUCTS, INC., a
California Corporation,
Alleged Bankrupt.

PETITION BY CREDITORS

To: The Honorable, the Judges of the United
States District Court for the Northern District
of California:

The Petition of Robert W. Gilbreth, doing business as Gilbreth Lumber Sales; Geo. H. Wilson, Incorporated, a corporation; and J. J. Graham, all of the County of Santa Cruz, District aforesaid, respectfully shows:

That Los Gatos Lumber Products, Inc., a California corporation, has had and maintained its principal place of business at 500 Mt. Herman Road, in the County of Santa Cruz, District aforesaid, for the longer portion of the six months next preceding the filing of this Petition than in any other place; that said Respondent is not a wage earner, nor a person chiefly engaged in farming or in the tillage of the soil, and owes debts to the amount of \$1,000.00 and over, and is insolvent.

That your Petitioners are and at all times herein

mentioned were creditors of said Respondent, having provable claims against said Respondent, and not contingent as to liability and liquidated as to amount, amounting in the aggregate in the excess of any securities held by them to the sum of Five Hundred Dollars (\$500.00) or over.

That Petitioner Robert W. Gilbreth is an individual doing business as Gilbreth Lumber Sales.

That Petitioner Geo. H. Wilson, Incorporated, is a corporation.

That Petitioner J. J. Graham is an individual.

That the nature and amounts of your Petitioners' said claims are as follows:

(a) A balance due from said Respondent to Gilbreth Lumber Sales upon an open, mutual, current and book account for lumber furnished by said Petitioner to said Respondent at its special instance and request, within four years last past, in the sum of \$281.71, no part of which has been paid, notwithstanding due demand therefor has been made.

(b) A balance due from said Respondent to Geo. H. Wilson, Incorporated, a corporation, upon an open, mutual, current and book account for goods, wares and merchandise furnished by said Petitioner to said Respondent at its special instance and request within four years last past, in the sum of \$176.37, no part of which has been paid, notwithstanding due demand therefor has been made.

(c) A balance from said Respondent to J. J. Graham for rent in the sum of \$750.00, no part of which has been paid, notwithstanding due demand therefor has been made.

Your Petitioners further represent that within four months next preceding the filing of this Petition, said Los Gatos Lumber Products, Inc., committed an act of bankruptcy in that on or about the 19th day of December, 1956, said Los Gatos Lumber Products, Inc., made or suffered to be made a preferential transfer as defined in Subdivision a, Section 60, of the Bankruptcy Act, in that it made, executed and delivered to Paul Gammill, Sr., and Paul Gammill, Jr., who were then and there wholly unsecured general creditors, a mortgage of personal property belonging to Los Gatos Lumber Products, Inc., on account of an antecedent indebtedness.

Wherefore, your Petitioners pray that service of this Petition with subpoena be made upon said Respondent, Los Gatos Lumber Products, Inc., a California corporation, as provided in the Bankruptcy Act, in that said Respondent may be by this Court adjudged to be a Bankrupt within the purview of said Act.

ROBERT W. GILBRETH,
Individual Doing Business as Gilbreth Lumber
Sales;

GEO. H. WILSON, INCORPORATED,
A Corporation;

J. J. GRAHAM,

By /s/ DANIEL ARONSON, JR.,
 Their Attorney in Fact.

Duly verified.

[Endorsed]: Filed January 22, 1957, US.D.C.

[Title of District Court and Cause.]

STATEMENT OF AFFAIRS

Summary of Debts and Assets

(From the statement of the debtor in Schedules A and B.)

Schedule A.

1-a. Wages	\$ 2,844.44
1-b. (1) Taxes due United States	5,903.82
1-b. (2) Taxes due States	1,220.94
1-b. (3) Taxes due Counties, Districts and Municipalities	2,606.73
1-c. (1) Debts due any person including the United States, having priority by laws of the United States	None
1-c. (2) Rent having priority	None
2. Secured claims	118,049.29
3. Unsecured claims	208,154.77
4. Notes and bills which ought to be paid by other parties thereto	None
5. Accommodation paper	None
Schedule A, total	\$338,779.99

Schedule B.

1. Real Estate	\$ 46,498.08
2-a. Cash on hand	None
2-b. Negotiable and non-negotiable instruments and securities	None
2-c. Stock in trade	1,345.58

Schedule B.

2-d. Household goods	None
2-e. Books, prints and pictures	None
2-f. Horses, cows and other animals	None
2-g. Automobiles and other vehicles	2,750.00
2-h. Farming stock and implements	None
2-i. Shipping and shares in vessels	None
2-j. Machinery, fixtures, and tools	141,333.80
2-k. Patents, copyrights and trade-marks	None
2-l. Other personal property	None
3-a. Debts due on open accounts	3,495.64
3-b. Policies of insurance	None
3-c. Unliquidated claims	None
3-d. Deposits of money in banks and elsewhere.....	6,525.00
4. Property in reversion, remainder, expectancy, or trust	None
5. Property claimed as exempt	None
6. Books, deeds and papers	

Schedule B, total	\$201,948.10
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LOS GATOS LUMBER
PRODUCTS, INC.,

/s/ CARL MORTON,
Petitioner, President.

[Endorsed]: Filed May 13, 1957, U.S.D.C.

[Title of District Court and Cause.]

ORDER OF REFERENCE

A creditors' petition having been filed against the alleged bankrupt above named, and good cause appearing therefor,

Now, on motion of Messrs. Shapro & Rothschild, attorneys for the petitioning creditors herein,

It Is Hereby Ordered that the above-entitled proceedings be, and they are hereby referred to Hon. Bernard J. Abrott, one of the Referees in Bankruptcy, who shall be in charge thereof, and to Hon. Burton J. Wyman, as Referee in Bankruptcy, in the event said Hon. Bernard J. Abrott shall be unable to act, to take further proceedings herein in accordance with the provisions of the Bankruptcy Act; and

It Is Further Ordered that all notices required to be published in the above-entitled matter and all orders which the Court may direct to be published may be inserted in the "Watsonville Pajaronian," a newspaper published in the County of Santa Cruz, State of California, within the territorial district of this Court and in the county in which the bankrupt maintained its principal place of business.

Dated at San Francisco this day of February, 1957.

/s/ GEORGE B. HARRIS,
United States District Judge.

[Endorsed]: Filed February 26, 1957, U.S.D.C.

[Title of District Court and Cause.]

ORDER OF ADJUDICATION

Whereas, an involuntary petition in bankruptcy was filed in the above-entitled Court on the 22nd day of January, 1957, against Los Gatos Lumber

Products, Inc., a California corporation, praying that it be adjudged a bankrupt under the Acts of Congress relating to bankruptcy; and

Now, on the motion of Messrs. Shapro & Rothschild, attorneys for the Petitioning Creditors herein, and good cause appearing therefor,

It Is Hereby Ordered that said Los Gatos Lumber Products, Inc., a California corporation, be, and it is hereby adjudged a bankrupt.

Dated: This 29th day of March, 1957.

/s/ BERNARD J. ABROTT,
Referee in Bankruptcy.

[Endorsed]: Filed March 29, 1957, Referee.

[Endorsed]: Filed April 2, 1957, U.S.D.C.

[Title of District Court and Cause.]

ORDER TO SHOW CAUSE

Upon consideration of the annexed duly verified Trustee's Objection to the Proof of Secured Claim of Emmet L. Rittenhouse this date filed herein by Charles E. Hoppe, Trustee of the estate of the above-named bankrupt, and good cause appearing therefor,

It Is Hereby Ordered that Emmet L. Rittenhouse, Paul Gammill, Sr., and Paul Gammill, Jr., doing business as Gammill & Co., and each of them, do personally be and appear before Hon. Bernard J. Abrott, Referee in Bankruptcy, at his Court-

room, Room A, Civic Auditorium, Market and San Carlos Streets, San Jose, California, in said District, on the 17th day of January, 1958, at the hour of 2:00 o'clock p.m. of said day to show cause, if any there be, why the prayer of said Trustee's Objection should not be granted.

It Is Further Ordered that service of this Order may be made upon Respondents at any time not less than five (5) days prior to the return date hereof.

Dated at San Jose, in said District, this 3rd day of January, 1958.

/s/ BERNARD J. ABROTT,
Referee in Bankruptcy.

[Endorsed]: Filed January 8, 1958, Referee.

[Title of District Court and Cause.]

TRUSTEE'S OBJECTION TO THE PROOF
OF SECURED CLAIM OF EMMET L. RIT-
TENHOUSE

Comes now Charles E. Hoppe, the duly appointed, qualified and acting Trustee of the estate of the bankrupt above named and objects to the allowance herein that certain proof of secured claim heretofore filed herein by Emmet L. Rittenhouse, as Assignee of Gammill & Co., a co-partnership, in the sum of \$12,025.00, upon each and all of the following grounds:

I.

That by reason of the facts hereinafter alleged, said claimant received a preference voidable under the provisions of Section 60a and b of the Bankruptcy Act and under the provisions of Section 57g of said Act; therefore, said claim should not be allowed as a secured claim but only as a general unsecured claim.

II.

That the above-entitled proceedings were commenced herein by the filing of an involuntary petition against the above-named bankrupt on the 22nd day of January, 1957. That thereafter such proceedings were regularly and duly had in the above-entitled matter as that the undersigned, Charles E. Hoppe, was duly appointed as and thereafter duly qualified as and ever since has been and still is the duly appointed, qualified and acting Trustee of the estate of said bankrupt.

III.

That within four months next preceding the said 22nd day of January, 1957, and while said Los Gatos Lumber Products, Inc., a California corporation, was then and there insolvent, said bankrupt transferred a portion of its property to said claimant's Assignor, Paul Gammill, Sr., and Paul Gammill, Jr., doing business as Gammill & Co., in that more particularly and on the 3rd day of December, 1956, said bankrupt made, executed and delivered to said claimant's Assignor a mortgage of chattels covering certain of its personal property and which

said mortgage of chattels was thereafter and on the 19th day of December, 1956, recorded in Volume 1107, Official Records of Santa Cruz County, California, at page 586; that said mortgage was given without any current, or fair, consideration, and on account of an antecedent indebtedness. That said chattel mortgage was thereafter assigned to claimant herein by said Paul Gammill, Sr., and Paul Gammill, Jr., doing business as Gammill & Co.; that at the time of the aforesaid transfer claimant's Assignor was a general and wholly unsecured creditor of said bankrupt and that the effect of said transfer was to enable said claimant's Assignor to obtain a greater percentage of its debt than other then and now existing general and wholly unsecured creditors of said bankrupt; that at the time of said transfer said claimant's Assignor well knew and/or had reason to believe that the effect of said transfer would be to so enable said claimant's Assignor to obtain said preference.

IV.

In toto that said mortgage of chattels is invalid as against your Petitioner, as such Trustee, by reason of the unreasonable and unexplained delay between the date of execution thereof on December 3, 1956, and the date of recordation thereof on December 19, 1956.

V.

That other general and wholly unsecured creditors of said bankrupt have heretofore proved and filed herein their several proofs of claim and that

the assets of said bankrupt estate are insufficient to pay such unsecured claims of said creditors in full.

Wherefore, said Trustee prays that the foregoing objections to said proof of secured claim of said Emmet L. Rittenhouse, Assignee of Paul Gammill, Sr., and Paul Gammill, Jr., doing business as Gammill & Co., be, after due hearing, sustained; that said proof of secured claim be disallowed in toto as such and allowed herein only as a general unsecured claim; that said Trustee recover his costs and expenses herein incurred; or for such other, further and additional order as to this Honorable Court may seem proper in the premises.

/s/ CHARLES E. HOPPE,
Trustee.

SHAPRO & ROTHSCHILD,

By /s/ DANIEL ARONSON, JR.,
Attorneys for Trustee.

Duly verified.

[Endorsed]: Filed January 8, 1958, Referee.

[Title of District Court and Cause.]

FINDINGS OF FACT AND
CONCLUSIONS OF LAW

Emmet L. Rittenhouse having heretofore filed a secured claim in the sum of \$12,025.00 in the estate of the bankrupt above named and the Trustee hav-

ing filed objection to the proof of the said secured claim and issue thereon having been joined and a hearing upon the issues having been had by me on the 31st day of January, 1958, and thereafter regularly continued and concluded upon the 21st day of February, 1958, and evidence both oral and documentary having been submitted by the parties in interest and due consideration having been had thereon, I find as follows:

Findings of Fact

1. On the 22nd day of January, 1957, proceedings were commenced herein by the filing of an involuntary petition against the above-named bankrupt.

2. Between October 4, 1956, and December 3, 1956, and thereafter Gammill & Company, a co-partnership consisting of Paul Gammill, Sr., and Paul Gammill, Jr., advanced moneys and credit to the above-named bankrupt in a sum in excess of \$25,000.00.

On the third day of December, 1956, the above-named bankrupt signed a promissory note and chattel mortgage together with a Notice of Intended Mortgage of Chattels which notice recited that said corporation intended to mortgage to Gammill & Company certain machinery and equipment and other personal property and that the consideration therefor would be given on the 14th day of December, 1956. On the 14th day of December, 1956, the said note and chattel mortgage were delivered

to Gammill & Company. On the 14th day of December, 1956, Gammill & Company delivered the said notice and chattel mortgage to Emmet L. Rittenhouse, the claimant herein, pursuant to an assignment thereof dated December 3rd, 1956, and thereafter on December 19, 1956, the said chattel mortgage was duly recorded in the office of the County Recorder in and for the County of Santa Cruz.

3. The period of time elapsing between the 14th day of December, 1956, on which the said promissory note and chattel mortgage were executed by delivery and the 19th day of December, 1956, on which the said chattel mortgage was recorded, is not unreasonable.

4. On the 14th day of December, 1956, the records of the above-named bankrupt disclosed an item entitled, "Notes Payable Officers," totalling the sum of \$173,813.12. This item represented advances made by members of the family of Carl Morton, President of the Bankrupt corporation, which advances had been made at various times and in varying amounts but which in fact totalled the said sum of \$173,813.12. These sums were advanced to the corporation not as loans but as equity capital in the form of subscriptions to capital stock. Stock certificates were never issued by the Bankrupt corporation to the various members of the family of Carl Morton to evidence the said advances.

5. The fair market value of the property of the subject corporation on the 14th day of December, 1956, exceeded the liabilities of the corporation on that date. The net worth of the Bankrupt corporation on the 14th day of December, 1956, was approximately \$62,000.00.

6. Shortly prior to the 14th day of December, 1956, Paul Gammill, Sr., and Paul Gammill, Jr., inquired of Carl Morton in his capacity as president of the Bankrupt corporation and Patricia Morton in her capacity as the holder of \$82,568.32 of the item appearing in the balance sheet of the Bankrupt corporation as "Notes Payable Officers," and of George Stepovich, Esq., an attorney-at-law in his capacity as attorney for the Bankrupt corporation, as to the character of the apparent indebtedness of the Bankrupt corporation set forth in its balance sheet as "Notes Payable Officers" and totalling the sum of \$173,813.12. The said Paul Gammill, Sr., and Paul Gammill, Jr., were upon such inquiry advised that the said item of apparent indebtedness totalling \$173,813.12 did not represent a fixed indebtedness of the corporation but in fact represented equity capital of the corporation which was ultimately to be evidenced by the issue to the holders thereof of the capital stock of the corporation. The said Paul Gammill, Sr., and Paul Gammill, Jr., relied upon such advice and representation and their reliance thereon was reasonable.

7. Paul Gammill, Jr., and Paul Gammill, Sr., had no reasonable cause to believe that the Bank-

rupt corporation was not solvent on the 14th day of December, 1956.

8. The estate of the Bankrupt corporation is not sufficient to satisfy the claims of the unsecured creditors of the Bankrupt corporation and the allowance of the claimants chattel mortgage as a secured claim against the Bankrupt corporation will permit the claimant to secure a greater percentage of his claim than if such claim were held to be unsecured.

Conclusions of Law

1. The promissory note and mortgage of chattels securing the same created a valid secured obligation on the part of the bankrupt corporation to which by reason of a valid assignment the claimant, Emmet L. Rittenhouse, is now entitled.

2. The preference created by the subject promissory note and chattel mortgage is not voidable under the provisions of Sections 57g, 60a or 60b of the Bankruptcy Act or under any of them and such claims should, therefore, be allowed by the Trustee herein as a secured claim.

3. The bankrupt corporation was solvent within the meaning of Section 1(19) of the Bankruptcy Act on the 14th day of December, 1956, the date on which the subject promissory note and chattel mortgage were executed.

4. Paul Gammill, Sr., and Paul Gammill, Jr., a co-partnership doing business as Gammill & Company, the assignors of claimant of the subject

promissory note and chattel mortgage, had no reasonable cause on the 14th day of December, 1956, to believe the bankrupt corporation was insolvent within the meaning of Section 1(19) of the Bankruptcy Act.

Dated August 4, 1958.

/s/ BERNARD J. ABROTT,
Referee in Bankruptcy.

Affidavit of Service by Mail attached.

[Endorsed]: Filed August 4, 1958, Referee.

[Title of District Court and Cause.]

ORDER ALLOWING SECURED CLAIM

This matter coming on for hearing upon the proof of claim of Emmet L. Rittenhouse filed in the above-entitled cause and the objections of the trustee of the estate thereto and due notice of said hearing having been given to said claimant, and to the said trustee, and the said claimant and the trustee having appeared by counsel on said day, and evidence having been submitted and after hearing adverse interests,

It Is Ordered, that the objections of the trustee to the allowance of the proof of claim of said claimant be, and the same are hereby denied.

It Is Further Ordered that the claim of Emmet

L. Rittenhouse be, and it hereby is allowed as a secured debt in the amount of \$12,025.00.

Dated at Oakland, California, this 4th day of August, A.D. 1958.

/s/ BERNARD J. ABROTT,
Referee in Bankruptcy.

[Endorsed]: Filed August 4, 1958, Referee.

[Title of District Court and Cause.]

REFEREE'S CERTIFICATE ON PETITION
FOR REVIEW OF FINDINGS OF FACT
AND CONCLUSIONS OF LAW AND
ORDER ALLOWING SECURED CLAIM

The undersigned, one of the Referees in Bankruptcy, in accordance with the provisions of Section 39 a (8) of the Bankruptcy Act, hereby certifies as follows:

I.

Preliminary Proceedings

That on the 22nd day of January, 1957, an involuntary petition in bankruptcy was filed with the above-entitled Court against Los Gatos Lumber Products, Inc., a corporation, and on the 29th day of March, 1957, said Los Gatos Lumber Products, Inc., was duly adjudged bankrupt, and the matter was referred to the undersigned Referee to take

such further proceedings as might be required under the provisions of the Bankruptcy Act.

That thereafter, and on the 31st day of May, 1957, Charles E. Hoppe, of the City of San Jose, State of California, District aforesaid, was appointed Trustee of the estate of said bankrupt, and thereafter duly qualified as such Trustee.

That thereafter, and on the 8th day of January, 1958, Charles E. Hoppe, as such Trustee, filed with the above-entitled Court his Objections to the Proof of Secured Claim of Emmet L. Rittenhouse, and on the same day the undersigned Referee in Bankruptcy issued an Order to Show Cause on said Objections, which Order to Show Cause fixed the 17th day of January, 1958, as the date for the hearing of said Trustee's Objections (the original of which Objections and Order to Show Cause are forwarded herewith as part of this Certificate); that by stipulation between the parties and with the consent of the undersigned Referee in Bankruptcy, the hearing on the Order to Show Cause was continued from time to time.

That after hearing the evidence and considering the authorities, the undersigned Referee made his Findings of Fact and Conclusions of Law and Order Allowing Secured Claim on the 4th day of August, 1958 (the original of which Findings of Fact and Conclusions of Law and Order Allowing Secured Claim are forwarded herewith as part of this Certificate).

II.

Statement of Facts

The facts as developed on the hearings of said matter and as set forth in the Reporter's Transcript of said hearing (the original of which Reporter's Transcript is forwarded herewith as part of this Certificate) are:

Between October 4, 1956, and December 3, 1956, the date promissory note and mortgage of chattels hereinafter referred to bear, and after December 3, 1956, Claimant's assignors, Gammill & Company, advanced moneys and/or credit to Los Gatos Lumber Products, Inc., a California corporation, hereinafter referred to as the Corporation, in a sum in excess of \$25,000, one of the sources of such funds being from Cyril S. Kelly, Jr., and Marjorie G. Kelly, who desired to be paid by Gammill & Company the sums due them from Gammill & Company.

On December 3rd, 1956, the Corporation signed a promissory note and chattel mortgage, together with a Notice of Intended Mortgage of Chattels, which Notice recited that said Corporation intended to mortgage to Gammill & Company certain machinery and equipment and other personal property, and that the consideration therefor would be given on December 14th, 1956; that after said 14th day of December, 1956, said note and chattel mortgage, together with an assignment of same were delivered to this claimant, and that said chattel

mortgage was duly recorded on December 19th, 1956.

That at all times the Corporation was in need of additional working capital to carry on its business operations. Claimant's assignors knew of the need of the Corporation for additional working capital and assisted the Corporation in various efforts to obtain financing and were familiar with the value of the assets and equipment of the Corporation; and were advised at all times by the Corporation through its president, Carl Morton, Patricia Morton, the wife of Carl Morton, and the Corporation's attorney, George Stepovich, that the advances of capital made by members of the Morton family, totalling \$173,813.12, shown on the financial statements of the Corporation, were to be considered only as equity capital of the Corporation, and that said advances should be considered as stock of the Corporation held by members of the Morton family having made these advances.

III.

Hearings

At the time and places fixed for the hearing of said Trustee's Objections, there appeared before the undersigned, Daniel Aronson, Jr., Esq., of Shapro & Rothschild, San Francisco, California, for the Trustee, and Emmet L. Rittenhouse, Esq., of Santa Cruz, California, for the claimant. Said matter was heard and considered by the under-

signed upon the records and pleadings as herein-above set forth.

IV.

Referee's Findings

1. On the 22nd day of January, 1957, proceedings were commenced herein by the filing of an involuntary petition against the above-named bankrupt.

2. Between October 4, 1956, and December 3, 1956, and thereafter, Gammill & Company, a copartnership consisting of Paul Gammill, Sr., and Paul Gammill, Jr., advanced moneys and credit to the above-named bankrupt in a sum in excess of \$25,000.00.

On the third day of December, 1956, the above-named bankrupt signed a promissory note and chattel mortgage together with a Notice of Intended Mortgage of Chattels which notice recited that said corporation intended to mortgage to Gammill & Company certain machinery and equipment and other personal property and that the consideration therefor would be given on the 14th day of December, 1956. On the 14th day of December, 1956, said note and chattel mortgage were delivered to Gammill & Company. On the 14th day of December, 1956, Gammill & Company delivered the said note and chattel mortgage to Emmet L. Rittenhouse, the claimant herein, pursuant to an assignment thereof dated December 3, 1956, and thereafter on December 19, 1956, the said chattel mortgage was duly re-

corded in the office of the County Recorder in and for the County of Santa Cruz.

3. The period of time elapsing between the 14th day of December, 1956, on which the said promissory note and chattel mortgage were executed by delivery and the 19th day of December, 1956, on which the said chattel mortgage was recorded, is not unreasonable.

4. On the 14th day of December, 1956, the records of the above-named bankrupt disclosed an item entitled, "Notes Payable Officers," totalling the sum of \$173,813.12. This item represented advances made by members of the family of Carl Morton, President of the Bankrupt corporation, which advances had been made at various times and in varying amounts, but which in fact, totalled the said sum of \$173,813.12. These sums were advanced to the corporation not as loans but as equity capital in the form of subscriptions to capital stock. Stock certificates were never issued by the bankrupt corporation to the various members of the family of Carl Morton to evidence the said advances.

5. The fair market value of the property of the subject corporation on the 14th day of December, 1956, exceeded the liabilities of the corporation on that date. The net worth of the bankrupt corporation on the 14th day of December, 1956, was approximately \$62,000.00.

6. Shortly prior to the 14th day of December, 1956, Paul Gammill, Sr., and Paul Gammill, Jr., in-

quired of Carl Morton in his capacity as president of the bankrupt corporation and Patricia Morton in her capacity as the holder of \$82,568.32 of the item appearing in the balance sheet of the bankrupt corporation as "Notes Payable Officers," and of George Stepovich, Esq., an attorney at law, in his capacity as attorney for the bankrupt corporation as to the character of the apparent indebtedness of the bankrupt corporation set forth in its balance sheet as "Notes Payable Officers" and totalling the sum of \$173,813.12. The said Paul Gammill, Sr., and Paul Gammill, Jr., were upon such inquiry, advised that the said item of apparent indebtedness totalling \$173,813.12 did not represent a fixed indebtedness of the corporation, but, in fact, represented equity capital of the corporation which was ultimately to be evidenced by the issue to the holders thereof of the capital stock of the corporation. The said Paul Gammill, Sr., and Paul Gammill, Jr., relied upon such advice and representation and their reliance thereon was reasonable.

7. Paul Gammill, Jr., and Paul Gammill, Sr., had no reasonable cause to believe that the bankrupt corporation was not solvent on the 14th day of December, 1956.

8. The estate of the bankrupt corporation is not sufficient to satisfy the claims of the unsecured creditors of the bankrupt corporation and the allowance of the claimants chattel mortgage as a secured claim against the bankrupt corporation will permit the claimant to secure a greater percentage

of his claim than if such claim were held to be unsecured.

V.

Statement of Question Presented

The question involved between the parties, which question, by his Order of August 4, 1958, the undersigned Referee answered in the negative, is:

“Is the Chattel Mortgage herein questioned, preferential within the meaning of Sections 60 a and b of the Bankruptcy Act?”

VI.

Petition for Review

That on the 29th day of August, 1958, and within the time allowed by the Court therefor, by an Order of the undersigned Referee in Bankruptcy, said Trustee, Charles E. Hoppe, filed his Petition for Review (which original Petition for Review is forwarded herewith as part of this Certificate) of the Undersigned Referee's Order Allowing Secured Claim.

VII.

Original Documents Accompanying Certificate

1. Trustee's Objections to Proof of Secured Claim of Emmet L. Rittenhouse, and Order to Show Cause issued thereon.

2. Findings of Fact and Conclusions of Law and Order Allowing Secured Claim.

3. Reporter's Transcript of Testimony.

4. Trustee's Exhibit No. 1—Balance Sheet as of July 31, 1956.

5. Trustee's Exhibit No. 2—Balance Sheet as of January 31, 1957.

6. Respondent's Exhibit No. 1—Voting Trust Agreement.

7. Respondent's Exhibit No. 2—Letter to Carl Morton.

8. Respondent's Exhibit No. 3—Appraisal.

9. Respondent's Exhibit No. 4—Portions of Small Business Administration Loan application.

10. Trustee's Opening Memorandum in Support of Objections to Proof of Secured Claim.

11. Claimant's Reply Memorandum to said Objections to Proof of Secured Claim.

12. Trustee's Closing Memorandum in Support of Objections to Proof of Secured Claim.

13. Petition for Review.

Dated at Oakland, California, in said District, this 24th day of November, 1958.

Respectfully submitted,

/s/ BERNARD J. ABROTT,
Referee in Bankruptcy.

[Endorsed]: Filed November 26, 1959, U.S.D.C.

[Title of District Court and Cause.]

NOTICE OF HEARING

Notice is Hereby Given that the Referee's Certificate on Petition to Review of Findings of Fact and Conclusions of Law and Order Allowing Secured Claim was forwarded to the Clerk of the above-entitled Court on the 25th day of November, 1958, and in the ordinary course of events should be on the calendar in the Post Office Building, San Francisco, California on the 15th day of December, 1958, at 9:30 o'clock a.m., under the provisions of Rules of Practice of District Court of the United States, Northern District of California (Bankruptcy Rules, Rule 10) effective April 1, 1955. It is suggested that Counsel representing the interested parties should check with the Clerk of the Court (Southern Division, at San Francisco) to make certain that said matter will come on for hearing on said above-mentioned date.

Dated: November 25, 1958.

/s/ BERNARD J. ABROTT,
Referee in Bankruptcy.

[Endorsed]: Filed November 25, 1958, Referee.

[Endorsed]: Filed November 26, 1958, U.S.D.C.

In the United States District Court for the Northern District of California, Southern Division

No. 47996—In Bankruptcy

In the Matter of

LOS GATOS LUMBER PRODUCTS, INC., a
California Corporation,

Bankrupt.

ORDER

The Trustee's petition for review raises questions of fact which were decided by the Referee on conflicting evidence. The Court cannot say that the findings of the Referee were "clearly erroneous" as that term is used in General Order 47. Therefore, the order of the Referee should be affirmed.

It is Ordered that the order of the Referee of August 4, 1958, be and the same is hereby affirmed.

Dated: December 19, 1958.

/s/ OLIVER J. CARTER,

United States District Judge.

[Endorsed]: Filed December 19, 1958, U.S.D.C.

[Title of District Court and Cause.]

NOTICE OF APPEAL

Notice is Hereby Given that Charles E. Hoppe, the duly appointed, qualified and acting Trustee of the estate of the above-named bankrupt hereby appeals the United States Court of Appeals for the Ninth Circuit from the Order of Honorable Oliver

J. Carter, Judge of the above-entitled Court, signed and filed herein on the 19th day of December, 1958, affirming the Order allowing secured claim made by Honorable Bernard J. Abrott, one of the Referees in Bankruptcy of the above-entitled Court on the 4th day of August, 1958, and from the whole thereof.

Dated at San Francisco, in said District, this 30th day of December, 1958.

SHAPRO & ROTHCHILD,

By /s/ DANIEL ARONSON, JR.,
Attorneys for Charles E. Hoppe, Trustee of the
Estate of Los Gatos Lumber Products, Inc.,
Bankrupt.

[Endorsed]: Filed December 31, 1958, U.S.D.C.

In the Southern Division of the United States District Court, for the Northern District of California

No. 47996—In Bankruptcy

In the Matter of

LOS GATOS LUMBER PRODUCTS, INC.,
Alleged Bankrupt

San Jose, California. January 31, 1958.

HEARING ON ORDER TO SHOW CAUSE
(Objection to Claim of Emmet L. Rittenhouse)

Before Hon. Bernard J. Abrott, Referee in Bankruptcy,

Appearances:

DANIEL ARONSON, JR, ESQ.,
SHAPRO AND ROTHSCILD,
For the Trustee.

EMMET L. RITTENHOUSE, ESQ.

The Court: In the Matter of Los Gatos Lumber Products, Inc.

Mr. Rittenhouse: Ready.

Mr. Aronson: Yes. Your Honor, this is an objection to proof of secured claim, the claim being filed by Emmet L. Rittenhouse, as the Assignee of Gammill & Co., a co-partnership. The objection is not to the allowance of the claim, but only to its allowance as a secured claim—the grounds being, No. 1, that there is a preference within the meaning of the Bankruptcy Act; and No. 2—unreasonable and unexplained delay between the date of execution and date it was filed before the hearing. The claim filed is not here. (Addressing Mr. Rittenhouse): Do you have the original?

Mr. Rittenhouse: I have the originals.

Mr. Aronson: We will introduce the copies; we don't have to prove up all the documents.

Mr. Rittenhouse: Stipulate they are all in order.

The Court: So there will be no misunderstanding that they are all in order you are still reserving one of the dates of the recordation?

Mr. Aronson: That they purport to be in the dates as indicated.

The Court: You gentlemen will stipulate, and identify the documents for the record.

Mr. Aronson: A promissory note, \$12,025.00, dated 12-3-56, executed—this is the note executed by the Central Coast Lumber Sales, Inc., to Cyril S. and Margery G. Kelly, guaranteed by Mr. Paul Gammill, Jr.; Mortgage of Chattels, dated December [1*] 3, 1956, executed by the Bankrupt to the Gammills, doing business as Gammill & Company, being recorded December 19, of 1956. Then there is the promissory note for \$12,025.00 also dated December 3, 1956, executed by the Bankrupt to the Gammill Company, or order, and the assignment of the promissory note and chattel mortgage from the Gammills to Mr. Rittenhouse——

Mr. Rittenhouse: As security——

Mr. Aronson: ——for the Kelly Company——

The Court: Date?

Mr. Aronson: December 3, 1956; it also bears a recording date of December 19, 1956. And the last document is an Affidavit of Publication of Intended Sale of Mortgage and Chattels, showing the date of Notice of Intended Sale—date of Publication. December 4, 1956.

The Court: Both of you gentlemen will stipulate that the documents will have the same effect as if received in evidence?

Mr. Rittenhouse: So stipulated.

Mr. Aronson: So stipulated. I will take up my case first. I will call Mr. Paul Gammill, Jr., under Section 21J.

***Page numbering appearing at top of page of original Reporter's Transcript of Record.**

PAUL GAMMILL, JR.

called as a witness on behalf of the Trustee, sworn and examined, testified as follows:

Direct Examination

By the Court:

Q. Your name is Paul Gammill, Jr.?

A. Yes.

Q. Is your address the same as when you were here before? A. Yes, sir. [2]

By Mr. Aronson:

Q. Mr. Gammill, you are one of the partners of Gammill & Company? A. Yes, sir.

Q. You are also connected with Central Coast Lumber Sales—you are an officer?

A. Right.

Q. And you are also connected with the sales?

A. The sales company?

Q. You are connected with a third business name, are you not?

A. Central Coast Lumber Sales, and Gammill & Company; as to the amount of stock held in Los Gatos Lumber Products, Inc.—

Q. But other than Los Gatos Lumber Products, Inc., there are just two; is that right?

A. That is right.

Q. Now you—when I refer to you, I am referring to the two companies specifically and not to you personally—over a period of time advanced, either by credit or by check, sums of money to the bankrupt? A. Right, sir.

(Testimony of Paul Gammill, Jr.)

Q. According to the claim filed by Mr. Rittenhouse, between October 4th and December 3rd, 1956, you advanced money to, or for the account, or for or on behalf of the bankrupt, for the purpose of assisting the bankrupt to stay in business until it was refinanced? A. Right, sir.

Q. Do you know the amount of money that was advanced during that period of time?

A. I can tell you the total amount advanced to Los Gatos Lumber Company from October 4th to January 15th—the last of our advances.

Q. What was that amount?

A. Approximately \$29,000.00. [3]

Q. Was that all by check?

A. That was all by check, yes, sir.

Q. I have all the checks and I have the totals; you are correct. The reason I wanted to know is that I ran a tape on the checks between the dates of October 4th and December 3rd of 1956—a total of \$25,381.26? A. Right.

Q. And then there were additional checks issued after that? A. Right, sir.

Q. And in addition to that you did business, did you not, with the bankrupt by lumber sales, not by money advances? A. By logging.

Q. Were you here at the examination of your father? A. It was my examination.

Q. Do you remember showing the books with the items during that time? By that I mean between October 4th and December 3rd.

A. No, sir, I don't. I can tell you approximately

(Testimony of Paul Gammill, Jr.)

from the inception of the logging company up to the end.

Q. How much was it?

A. Roughly \$28,000.00 in the logs.

Q. That is, you filed your claim for that?

A. Right; it was the Gammill Company that filed that.

Q. If I told you that during the period of October 4th to November 15th, from your books, it shows \$12,562.78—would you have any serious disagreement with that amount?

Mr. Rittenhouse: From whose books?

Mr. Aronson: From Gammill Company's books.

A. No—I don't understand.

Q. I say, from your examination a month or so ago, when you [4] had your books here, I abstracted the information from the books showing that from the first entry of October 4th to the last entry within the dates that I am concerned with right now, of November 15th, the total charges against the account of the bankrupt was \$12,562.78, which would be a portion of the \$28,000.00, would you say that would be approximately correct?

A. To my knowledge, I don't know; I just don't know all these things.

Q. But there was no question, Mr. Gammill, that by either money, or through logging operations, you extended credit or money to the bankrupt substantially in excess of \$12,000.00?

A. Right.

(Testimony of Paul Gammill, Jr.)

Q. And that was all done on an unsecured basis; you have no security?

A. Other than the chattel mortgage.

Q. Other than the question of the chattel mortgage that is here? A. Right.

Q. You obtained the chattel mortgage from the bank, and it is dated December 3rd; you have also a promissory note on that date. What were the circumstances leading up to the execution of the note and mortgage?

A. My cousin, Cyril Kelly, whom the company assigned the promissory note to, put up \$25,000.00, and my father and I put up \$25,000.00 to form the Central Coast Lumber Sales. Prior to that my father was engaged in the logging business. After forming a sales company and advancing money to the logging operations, my cousin, I would say in the latter part of November, wanted to get out of business. At that time we had advanced [5] considerable money to Los Gatos Lumber Products, and it was our knowledge at the time and we felt sure that an FHA loan would be granted to Los Gatos Lumber Products to whom we had advanced money; Kelly wanted his \$25,000.00 back, but since we had considerable money in the Los Gatos Lumber Products and in the logging operations, it would be impossible to give him the \$25,000.00 back in cash.

Q. Why would it be impossible?

A. Well, we had loaned most of the money to the Los Gatos Company.

(Testimony of Paul Gammill, Jr.)

Q. When you say it would be impossible for you, you mean Gammill Company?

A. Gammill Company. We had no intention of pressing the Los Gatos Lumber Products; we felt it would be refinanced, or later on sold, but in order to give Kelly some security to back the \$25,000.00, my father entered into negotiations back in Mississippi making it possible to get \$8,500.00 cash; we asked the Los Gatos Lumber Products to secure \$12,000.00 of the \$25,000.00 debt owing us, and also Kelly and we issued him a check of \$3,500.00, which would keep the business together; in other words, it wouldn't pull it apart.

Q. Did you ask the bankrupt for the payment of \$25,000.00, \$12,000.00, or any sum at all to pay Kelly his money?

A. No; we didn't; we just asked for security.

Q. Why didn't you ask for it?

A. We had everything to lose in that respect; we felt the [6] business was a going concern and we felt that capital would be granted by an FHA loan.

Q. You felt they were solvent?

A. Yes, sir.

Q. You knew that they were seeking refinance?

A. Right—without participating in it.

Q. You were closely associated in that direction?

A. Right.

Q. You knew that they were seeking refinancing from the Small Business Administration?

A. Right.

(Testimony of Paul Gammill, Jr.)

Q. And that they didn't have the cash; as a matter of fact they couldn't—

A. They didn't have the absolute cash, but as far as assets and liabilities, I considered them solvent.

Q. Didn't you oppose the giving of the mortgage by the bankrupt, Mr. Gammill?

A. Oppose it?

Q. On the basis that it would interfere with the financing operation of the FHA loan?

A. No, sir; I didn't.

Q. You didn't? A. No, sir.

Q. Who went to the bankrupt to ask for the promissory note; did you, or Mr. Kelly, or Mr. Rittenhouse, or your father—or who was it?

A. Well, it was quite a group; there was my cousin, Dave Gammill, I believe my father, Sid. Kelly, Mr. Rittenhouse here, and Mr. Bennett, who was the attorney acting at that time for the Gammills, and myself.

Q. (By Mr. Rittenhouse): Was there any discussion at that time of the financial condition of the bankrupt?

A. I think I was well aware of the condition of the company— [7] if you could put it that way; we discussed it at length about the chattel mortgage and no one felt it would hurt the business as far as any future sale—it wasn't as if we had asked for a total indebtedness loan.

Q. How was the sum of \$12,025.00 reached?

A. I think I mentioned that Kelly had \$25,-

(Testimony of Paul Gammill, Jr.)

000.00 in it and he wanted the amount coming to him back. Having invested most of our money in the Los Gatos Lumber Products—in our own company, and money loaned to Los Gatos Lumber Products—in order to continue our operation; we also hoped to continue loaning funds to Los Gatos Lumber Products, advancing funds, and we couldn't give Mr. Kelly any \$22,000.00, so the figure of \$12,-000.00 was reached, and my father put up an additional \$8,500.00, which would make roughly \$20,-000.00, and Central Coast Lumber Sales issued a check for, I believe, \$2,300.00 to bring it up to the \$22,000.00 of Kelly's investment.

Q. At this time were you an officer and director of the bankrupt? A. No, sir.

Q. When did you cease being an officer of record?

A. In April, I believe it was April 2nd, 1956.

Q. If I understand your testimony you say that you had every reason to believe the bankrupt was solvent at that time?

A. Well, I would say it was solvent, yes, sir; I felt that through a sale, or the possibility of re-financing, and our advancing money it would carry on quite successfully?

Q. At about December 3rd, 1956——

A. I would class it as [8] solvent.

Q. By "solvent," what do you mean?

A. That the assets would exceed the liabilities.

Q. You believe that? A. Yes, sir.

(Testimony of Paul Gammill, Jr.)

Q. And you believe they were perfectly capable of continuing business?

A. Well, with additional finance, yes.

Q. With additional finance?

A. Well, in that respect I am speaking of the current small advances we were making.

Q. I am talking about the over-all picture. You knew there was a necessity for the refinancing and obtaining the loan to stay in business?

A. To stay in business, yes.

Q. The lumber operation was not in very good shape in December, 1956?

A. It was not at its best at the end of any year, but it was better than it was at the beginning of 1957.

Q. As a matter of fact, around the same time that these transactions took place you were collecting the accounts receivable of the bankrupt, weren't you?

A. No, sir; I never collected money.

Q. You attempted to?

A. I attempted to, yes.

Mr. Aronson: I think I have nothing further of Mr. Gammill at this time.

Mr. Rittenhouse: If I may, I would like to examine Mr. Gammill now.

The Court: Yes, Mr. Rittenhouse. [9]

(Testimony of Paul Gammill, Jr.)

Cross-Examination

By Mr. Rittenhouse:

Q. Mr. Gammill, during the negotiations before December 30, 1956, leading up to the 3rd of December, 1956, you were represented by a Mr. Bennett—Attorney Bennett? A. Right, sir.

Q. And at that time I was urging the claim of Mr. Kelly and his mother, Mrs. Kelly, is that correct? A. Yes, sir.

Q. And on or about December 3rd we arrived at a solution for the settlement of that particular claim? A. Yes.

Q. These papers, or these documents, represent that; is that correct? A. Yes, sir.

Q. The balance of the \$12,025.00 and \$10,800.00 represent the balance, unpaid balance due from you and your father to Mr. Kelly and his mother?

A. That is right.

Q. Now, in order to satisfy Mr. Rittenhouse and his client, you secured for my satisfaction this assignment, rather this chattel mortgage and the note which was later on assigned to me in trust for the purpose of applying any proceeds onto the debt that was due from you to the Kellys; that is correct, isn't it? A. Right, sir.

Q. Now, we discussed the matter of publication of notice under Section 3440 of the Civil Code specifically, didn't we? A. Yes, sir.

Q. (By Mr. Aronson): Were these conversa-

(Testimony of Paul Gammill, Jr.)

tions in the presence of Mr. Morton or some other representative of the bankrupt?

A. No; they weren't; Mr. Morton was never at any of these [10] conferences.

Mr. Aronson: Then I object to that as incompetent, irrelevant, and immaterial.

Q. (By Mr. Rittenhouse): Well, in any event, the Exhibit here—which is the Affidavit of Publication, and which is in evidence, shows that this transaction was to be consummated on the 14th day of December.

Mr. Aronson: I can make it very simple for you as far as that is concerned, Mr. Rittenhouse, and there need be no testimony, because the documents speak for themselves.

Mr. Rittenhouse: I wanted it in the record.

Mr. Aronson: Merely the requirement of publication of such notice and not lack of explanation of publication—it is purely a matter of law as to whether there was a delay; the documents speak for themselves.

Mr. Rittenhouse: I want to bring out that the mortgages were to be delivered on the 14th day of December, 1956, with reference to their recording date in the next week which accounts for the delay, and which is one of his points. The 14th was a Friday.

Mr. Aronson: Hearsay.

Q. (By Mr. Rittenhouse): Now, with reference to your opinion as to the solvency of this particular Los Gatos Lumber Products Company, Mr. Gam-

(Testimony of Paul Gammill, Jr.)

mill, did you have occasion on October 8th, 1956, to have an appraisal, or to see an appraisal of the assets of this particular company?

A. Yes, sir.

Q. Might I show you this particular document and ask you if you [11] have seen anything like that before?

A. Yes, sir; different form, yes, sir.

Q. Why was this made?

A. To determine the appraisal value for the Small Business Administration.

Q. Who made the appraisal?

A. California Appraisal Company.

Q. Did you assist in the appraisal in any way?

A. No, sir; I didn't; I was present during the signing of this particular——

Q. (By Mr. Aronson): Was this document you are referring to made for the bankrupt?

A. Right, sir.

Q. I mean, did the bankrupt cause it to be made?

Mr. Rittenhouse: At the time of this particular reference to the Small Business Administration, or small business deal.

Q. (By Mr. Rittenhouse): Now, with reference to recapitulation, what are the total values of the assets of this particular operation, without regard to their inventories or cash or various things of that nature?

Mr. Aronson: Are you going to read from that? (Indicating document.)

(Testimony of Paul Gammill, Jr.)

A. Yes.

Mr. Aronson: I object to it as incompetent, irrelevant, and immaterial.

Mr. Rittenhouse: What do you want me to do—call the appraiser down here? (Discussion.)

The Court: On the record. Let the record show that there is now marked for identification an appraisal, Los Gatos Lumber [12] Products Company; it was accompanied by a document on the letterhead of California Appraisal Company, and is dated October 8th, 1956—and when I say “marked for identification,” that is without prejudice to either the petitioner or the respondent to offer it in evidence.

Q. (By Mr. Rittenhouse): Your testimony was that you saw the original of this document?

A. Yes, sir.

Q. And the values made by this appraisal form, as set forth in the recapitulation of the assets, excluding the inventory and cash, are as follows; is that correct? A. Right, sir.

Q. In other words—new recapitulation values, \$199,350.35? A. Correct.

Q. Sound values, \$173,506.11; insurable values, \$160,900.25. I will ask you whether or not we might also go through the same routine with this particular document as with this one; it is a financial statement as of July, 1956?

Mr. Aronson: Prepared by the bankrupt?

Mr. Rittenhouse: Prepared by American Audit

(Testimony of Paul Gammill, Jr.)

Company at the request of the bankrupt corporation.

Mr. Aronson: If they are the same.

The Court: For identification.

Q. (By Mr. Rittenhouse): Did you ever see this document before? A. Yes, sir.

Q. Did you see it on or before these advances were made—say, in August, 1956?

A. Prior to the advances, yes. I don't know the exact date I saw it, but it was in the neighborhood. [13]

Q. And the total asset value set forth by this particular document is \$249,516.52?

A. Yes, sir.

Q. Now, with reference to the fixed liabilities there is a notation there of \$173,813.12?

A. Yes, sir.

Q. What did that represent?

A. Well, that represented—I don't know about the total amount but that particular figure represents moneys advanced to the corporation.

The Court: Let the record show that the Court has interrupted Mr. Rittenhouse's examination of Mr. Gammill, Jr., to afford counsel for the petitioner or respondent an opportunity to call Mr. Morton.

CARL MORTON

called as a witness on behalf of the Trustee, sworn and examined, testified as follows:

Direct Examination

The Court: What is your full name?

A. Carl Morton.

Q. And your address is still La Jolla?

A. 1706 Harrison.

By Mr. Aronson:

Q. You were the president of the bankrupt corporation? A. That is right.

Q. Did you have occasion to have a conversation with the Gammills and Kellys in December, 1956?

A. Right.

Q. What was the substance of that conversation?

A. Well, in essence, Sid Kelly desired to leave the business——

Mr. Rittenhouse: Identify your business. [14]

A. Well, he desired to leave Central Coast Lumber Sales which he was tied in with Mr. Gammill, Jr., of the company—and he simply wanted “out,” and he wanted his money back.

Q. Did they ask you for the money?

A. No.

Q. Did they ask you only for the chattel mortgage?

A. We discussed it at some length, and that was the upshot of the method of technique in this particular instance where Kelly was involved.

(Testimony of Carl Morton.)

Q. Was there a discussion of your ability to pay cash?

A. Yes; I think there was because it was common knowledge; we had discussed this at some length as to what our cash finances were.

Q. So it was decided that you were giving Kelly a chattel mortgage to secure a portion of your indebtedness?

A. This was the method we arrived at—some payment of cash—and to keep our business.

Q. And the mortgage was given as security for money previously advanced? A. Yes.

Q. Was there any objection to the giving of the mortgage?

A. We didn't want to do it—I say “we,” because we discussed it among ourselves. Mr. Gammill, Jr., and I discussed it. We knew that possibly a chattel mortgage might jeopardize our getting a loan from the Small Business Administration; it wasn't desirous but under the circumstances, with the advocacy of Sid Kelly, it was the only out.

Q. In other words, there was a discussion between you and Mr. [15] Gammill, Jr., as to the inadvisability of giving the mortgage at that time?

A. If you want to call it inadvisability, or lack of desirability, either one.

Q. But there was discussion as to the giving of the mortgage? A. Yes.

Q. And it was because of the reason you stated—the possible jeopardy of the refinance; you were the president of the company—— A. Yes.

Q. Let me ask the whole question——

A. All right.

(Testimony of Carl Morton.)

Q. I want to ask you what your financial condition was at the giving of this mortgage on December 3rd of 1956, referring to your insolvency by definition, the question of the excess of liabilities over assets, or assets over liabilities?

A. Well, as indicated in the appraisal—can I use these——

Mr. Aronson: Yes.

A. The appraisal and the financial statement indicated we had a good deal in excess of our liabilities; but also a very obvious fact to us was that we didn't have adequate capital to carry the——

Q. I am not asking you what was indicated; I am asking you what you knew of the business as of assets and liabilities in December, 1956?

A. Yes—I am talking about fixed assets, current assets—the whole kit and caboodle; I considered it solvent.

Q. You considered it solvent—you didn't consider it insolvent?

A. No—but for lack of working capital, a few minor operations [16] such as resawing, and preparing lumber for sale——

Q. It didn't increase your liabilities or decrease them?

A. In the month of December, yes, it did decrease our liabilities to this extent: We were utilizing an inventory that was an asset; we were selling inventory, a two-year depreciation inventory; at the same time we were paying out for wages and so forth, and we did not at that time have addi-

(Testimony of Carl Morton.)

tional logs coming in and additional lumber; it did double it.

Q. Did you operate at a profit or loss between January, 1956, and '57?

A. I don't know the exact figures, but my guess would be that we operated at a loss, because a mill has to operate at pretty full speed in order to make money.

Q. When you made money you paid bills with it?

A. Yes.

The Court: Mr. Morton, I want you to forget about working capital, and attempting to obtain a loan for small business or anyone else. In your opinion, in the event the assets of the bankrupt corporation were liquidated—ordinary liquidation—at the time this document was given to secure a creditor, in your opinion would the assets have been more or less than the obligations?

A. Substantially more.

Q. And that is the reason you say that in your opinion the bankrupt was solvent?

A. Yes, sir; as a side line, if I may say so—we were negotiating a short time later for a sale of the company at \$126,000.00 and were very close to a consummation of that particular sale. [17] This sale would have paid off all creditors except myself and my family, as far as their indebtedness was concerned.

Q. Now, you are familiar with the schedules filed?

A. Yes.

Q. And they were filed as of January 22, 1957.

(Testimony of Carl Morton.)

You are also familiar with the assets and liabilities? A. Yes.

Q. Did you have a belief that the condition was other than it was in December, or substantially the same in December? A. I would say yes.

Q. You believed it was better?

A. No; substantially the same.

Q. And this balance sheet marked for identification, are you familiar with that?

A. Balance sheet? This one was prepared January 31, 1957; I believe we prepared this ourselves from the books, didn't we?

Q. If you don't know, say so.

A. I don't know.

Q. (By Mr. Aronson): You didn't have that in December, 1956?

A. No; this was prepared during the sale.

Q. So all you have is the last balance sheet—July 31st of 1956 plus a knowledge of the operation of the business in the intervening period that you operated the business between you?

A. Yes.

Q. I show you a document. (The document is examined by the witness.)

Q. After looking at that document, do you still want to tell the Court that you believe it is solvent, and that its assets substantially exceed its [18] liabilities?

A. I took into account in that statement two amounts——

Mr. Rittenhouse: Here are three amounts.

(Testimony of Carl Morton.)

The Witness: Two amounts—the figures of notes payable to officers were not going to be urged.

Q. It was a debt, though?

A. It was.

Q. Still owing, isn't it, Mr. Morton?

A. Yes.

Q. It is being urged now, isn't it; you filed a claim in these proceedings, did you not?

A. Yes—of course, I did.

Q. It was then, and is now, a liability of the corporation and is reflected in the balance sheet and was made available to the Gammills; they knew it?

A. Yes, sir.

Q. As a matter of fact, you continued to operate as a deficit until July 31, 1956, the date of that balance sheet, did you not?

A. Well, this is one that shows a profit here. In the past we made a profit when we were able to operate.

Q. I am not sure you understood my question—

A. You said from July 31st did we make a profit; I can't answer that now. If I didn't have an accountant's record month by month my opinion is we were not making it.

Q. Your opinion is that you were working at a substantial deficit?

A. Do you mean based solely upon an income statement?

Q. No; solely upon the operation of business; you were losing money, weren't you? [19]

(Testimony of Carl Morton.)

A. Well, look, we had fixed debts upon the equipment; we are not disregarding those. If you operate from a profit-and-loss standpoint it wouldn't be a profit. Does that answer the question?

Q. Taking everything into consideration you couldn't pay your bills? A. That's right.

Q. Your bills were mounting up?

A. That's right.

Q. You owed—in a period of two months you incurred an indebtedness to the Gammills in excess of \$25,000.00, didn't you?

A. Some of those were being liquidated right along; you realize, of course, out of the inventory.

Q. I show you a balance sheet of July 31st; there is a deficit shown of sixty-six odd thousand dollars? A. Yes.

Q. I show you one of January 31st, 1957, to the date of—at the bottom—you have a deficit on November 1, 1956—what is that amount?

A. It reads \$132,053.52.

Q. Would that refresh your recollection as to the status of your business?

A. I would say yes.

Q. You knew, did you not, Mr. Morton, that your liabilities far exceeded the value of the assets, that they were substantially less than the amount of your liabilities, didn't you? I am referring to the first of December——

A. Are you taking into account the notes payable to officers?

(Testimony of Carl Morton.)

Q. Everything. A. Yes.

The Court: You already knew at that time that trying to obtain additional finances through the Small Business Administration or somebody else—you still couldn't continue to [20] operate; isn't that right? A. Quite right.

Q. And Mr. Gammill was a part of these negotiations? A. Yes.

Q. And he attended meetings with Small Business Administration people? A. Right.

Q. And he had the same knowledge that you had, didn't he? A. Yes.

Mr. Aronson: On this particular key point I have nothing further, your Honor. If I may proceed, there are a couple of other elements that are necessary to prove my case—I mean from Mr. Morton.

The Court: You mean now?

Mr. Aronson: May I make the suggestion that perhaps Mr. Rittenhouse and I can stipulate to these other matters—that there are other creditors who will receive substantially nothing from these proceedings——

Mr. Rittenhouse: I don't know anything about what the records show, so I would be unable to stipulate to that. (Discussion.)

Mr. Aronson: I think I can cover this proof without Mr. Morton or anybody else. As of December 1st, 1957, the Trustee had on hand \$17,115.16. Now there have been no substantial payments since then; it might be slightly less by small items. There

(Testimony of Carl Morton.)

are on file—in fact the claims are in the file and I have made a list and have run a tape, and the total is 75 claims filed as far as I know. Roughly, there are priority labor claims, \$1,799.18; expense of administration wage claims, \$1,296.46; tax claims, \$9,641.38; secured claims, \$22,148.62; [21] unsecured claims, \$320,275.93. Now this total doesn't include anything in the nature of the \$12,000.00 claim here being opposed. I haven't added the figures up but it is substantially more than the Trustee has on hand.

The Court: There are no further matters, to the knowledge of the Trustee in these proceedings, so this is the sole one to be disposed of. Possibly an adjustment may be necessary upon the sale, which would be charged against the estate because it is a shortage, not an overage; so, gentlemen, the unsecured creditors would receive virtually nothing in these proceedings. Do you want to carry this on the calendar? If not, I am going to excuse Mr. Morton.

Mr. Rittenhouse: I have some questions I want to ask him.

(Discussion concerning an agreeable date for continuance.)

The Court: Continued to February 21, at 2:00 p.m. [22]

[Title of District Court and Cause.]

FURTHER HEARING ON ORDER, ETC.

The Court: In the Matter of Los Gatos Lumber Products, Inc.

CARL MORTON

called as a witness on behalf of the Trustee, having been previously sworn by the Court, further testified as follows:

Direct Examination

By Mr. Aronson:

Q. Do you have the two balance sheets that you have referred to?

Mr. Rittenhouse: I think that this appraisal is in the picture; I think this July 31st balance sheet was the one.

Q. (By Mr. Aronson): Mr. Morton, at the last hearing reference was made to a balance sheet of the bankrupt corporation which was dated July 31, 1956, and if I remember correctly you testified that you and Messrs. Gammill relied in part upon this balance [23] sheet to determine the financial status of the corporation; is that correct?

A. I am not sure, but I believe we discussed it that way.

Q. Well, whether or not it was discussed—is that true? A. Yes.

Q. There have been numerous pencil notations made on this. Do you know who put this on there?

A. Yes; I did.

(Testimony of Carl Morton.)

Q. You did.

Mr. Aronson: We will offer this balance sheet in evidence, your Honor. (Addressing Mr. Rittenhouse.) Can it be pulled out?

Mr. Rittenhouse: You mean just the balance sheet? This was an audit prepared by the——

The Witness: American Audit Company; yes.

Q. (By Mr. Rittenhouse): This represents a copy of the original, Mr. Morton?

A. This would constitute an original, I guess.

Mr. Aronson: Well, put the whole document in.

The Court: Trustee's No. 1 of this date. (Audit by American Audit Co.)

Q. (By Mr. Aronson): You also made reference to another financial statement which was dated January 31, 1957.

Mr. Rittenhouse: Yes—this one here.

Mr. Aronson: As of January 31, 1957. You referred to that at the last hearing; is that correct?

A. Yes.

Mr. Aronson: We will offer that as our next Exhibit in order, your Honor.

The Court: Trustee's No. 2 of this date. (Financial Statement, [24] January 31, 1957).

Q. (By Mr. Aronson): Is it still your testimony, Mr. Morton, that the bankrupt corporation was solvent in the sense as we discussed last time—that is, the excess of assets over liabilities between the months of October and December, 1956?

A. Yes.

Q. It still is your testimony?

A. Yes.

(Testimony of Carl Morton.)

Q. In spite of the fact that you have in front of you the Exhibits—balance sheets, which show a substantial deficit? A. Yes.

Q. Will you explain to the Court how you reached the conclusion that they were obviously wrong?

A. You mean you want me to explain why the corporation was solvent?

Q. Yes.

A. Because as far back as of April, I believe, 1956, we realized we would need additional financing, and we had discussed and agreed that the notes of the two officers would be cancelled and taken in the form of equity stock.

Q. When you say "we," who do you mean?

A. My family—my wife, my former wife, and my mother and myself.

Q. Is that the total of the \$173,000.00 figure?

A. No.

Q. Who else is involved?

A. Hughston, my uncle, didn't agree to that at this time; he wanted the notes to stand up; the rest had agreed, and at a later date my uncle did agree.

Q. Just as to what did they agree?

A. They agreed to take equity stock in the company in lieu of [25] notes.

Q. That would still be a liability to the company, would it not?

A. That is, equity capital? Yes.

Q. They didn't waive anything, did they—or did they?

(Testimony of Carl Morton.)

A. There is a difference between the notes and liability; they waived the notes and took capital stock.

Q. They didn't waive the obligation, did they; did they ever tell either Mr. Gammill, Mr. Kelly, or Mr. Rittenhouse that they waived the money that was owed to them?

A. No; they didn't say it in those words; the only thing they agreed to was to take equity, capital stock in lieu of notes.

Q. They were going to take \$173,000 in stock?

A. Yes.

Q. That was in refinancing the corporation?

A. This would have been in refinancing the corporation, that is right.

Q. And the refinancing situation was to be handled through the Small Business Administration?

A. No; in August, for instance, I went to Colorado; we realized we needed additional financing——

Q. I don't want to cut you short, but in October, November, and December, you were working for a Small Business Administration loan?

A. Yes.

Q. And that was the refinancing you were concerned about? A. At that time.

Q. At that time, yes; and Mr. Gammill was completely familiar with that situation?

A. Yes. [26]

Q. And it is also true, is it not, Mr. Morton,

(Testimony of Carl Morton.)

it would have been impossible for you to continue the business if you did not get that?

A. If we did not get additional funds.

Q. And the Small Business Administration loan; you were operating on a deficit?

A. You are pinning it down—when you say additional funds.

Q. But at that time, October, 1956, the only source of additional funds available was the application to Small Business Administration?

A. Up to and at the time the funds became available from the Gammill organization.

Q. You mean money became available from Gammill?

A. In the form of advances.

Q. Yes. I am talking about that period; during that period is when you applied for a Small Business Administration loan? A. That is right.

Q. But you knew at that time you couldn't continue without a Small Business Administration loan or from some other source? A. Yes.

Q. You operated on a deficit?

A. For two months—not too much earlier.

The Court: Mr. Morton—so I will understand your answer—you previously testified that you and the others that you mentioned were willing to take equity capital?

A. In other words, common stock in lieu of notes.

Q. When you use the word “equity,” now am I to reach the conclusion that in the event there

(Testimony of Carl Morton.)

was no equity there would be [27] no obligation of Los Gatos Lumber Products, Inc., to pay off these obligations of you and these others that you mentioned?

A. I think, your Honor, you are going into something there——

Q. Tell me, in your own words, just what you and the others that you mentioned agreed to; you said that finally your uncle was the last one to agree, and that prior thereto you and the others had agreed to take equity stock—and I am trying to find out what you had in mind when you made that statement. If Los Gatos Lumber Products, Inc., was insolvent and went into bankruptcy, would there be any obligation on you people to pay anything?

A. If we had gone ahead and accomplished what we had agreed to then I presume we would just take the position of stock owners.

Q. And in the event you didn't obtain money on a Small Business Administration loan or from some other source, then what would your status be with reference to being a creditor, or having an obligation (due you) as a stock owner?

A. As a note holder, or stock holder ?

Q. Yes.

A. It would stay the same, I presume.

(Testimony of Carl Morton.)

Cross-Examination

By Mr. Rittenhouse:

Q. Now, Mr. Morton, I am going to show you a document dated January 7, 1955, and ask you whether or not you recognize this document?

A. I do.

Q. And ask you whether or not that is your signature on the second page of the document?

A. It is.

Q. Is that the signature of Mrs. Gammill, Jr., and one of Mr. [28] Parsons? A. Yes.

Q. When was this secured—on the date that it bears? A. The date that it bears.

Q. Was that secured by you?

A. Yes, my company's lawyer drew this up at the time we originally issued stock, the purpose being to give me a voting trust to control the stock—the stock that went to Edward Parsons.

Mr. Aronson: I will object to the testimony as being incompetent, irrelevant and immaterial.

Mr. Rittenhouse: I offer it in evidence; the purpose of the introduction, your Honor, is to show that this man, Mr. Morton, was at all times in control of the corporation. (Addressing the witness.) That document of trust was never revoked at any time?

A. No.

The Court: Respondent's No. 1.

Q. (By Mr. Rittenhouse): I show you a docu-

(Testimony of Carl Morton.)

ment dated April 23, 1956, which is signed "Paul," with reference to both sides. Do you recognize this document? A. Yes.

Q. Who is "Paul"?

A. He is my stepfather.

Q. With reference to the writing on the back side? A. That is my mother's.

Q. Did you receive that on or about the date it bears? A. Yes.

Mr. Rittenhouse: We offer this in evidence.

Mr. Aronson: To which we object; it is incompetent, irrelevant and immaterial; too remote in time.

Mr. Rittenhouse: The purpose of it is to show the intent of [29] his mother with reference to the \$10,000.00 she advanced, the very time she advanced it as being equity Capital for the issuance of stock.

The Court: I will mark it for indentification, Respondent's No. 2, and for the record, Mr. Morton, what is the last name of "Paul"?

A. Willer-vetersen.

Q. (By Mr. Rittenhouse): In September—maybe I should ask also with reference to the writing on this back page: What is your mother's last name? A. Ada Willer-vetersen.

Q. Maiden name?

A. Ada Whiteside Peterson.

Q. With reference to September, 1956; September and October of 1956: Did you have any reason to have your properties—that is not your properties,

(Testimony of Carl Morton.)

but the properties of the bankrupt corporation appraised? A. Yes.

Q. And do you have an opinion as to their value at that particular time?

A. What appraisal is that?

Q. Your opinion as to——

A. My opinion as to the validity of the appraisal?

Q. No—your opinion as to the value of the assets of the corporation? A. Yes.

Q. And would you express that opinion?

A. The physical assets of the corporation?

Q. Yes, physical assets.

A. Well, as shown in the recapitulation of the appraisal made by California Appraisal Company, I believe the figures arrived at there to be thorough and correct as of that time. [30]

Q. And what were the figures?

The Court: Do you have the appraisal, Mr. Rittenhouse?

Mr. Rittenhouse: I have a copy, and I believe the Trustee has one of the originals.

The Court: I wonder if Mr. Aronson would object, on the copy—I would sooner have the document before I hear Mr. Morton's interpretation of the document.

Mr. Rittenhouse: I will offer this in evidence.

Mr. Aronson: I will object to it as incompetent, irrelevant, and immaterial.

The Court: What is the date of the appraisal?

(Testimony of Carl Morton.)

A. The date on the covering letter is October 8, 1956.

The Court: And the date of the alleged preferential between? A. October 4th.

The Court: The Trustee alleges that the preference was created on December 3, 1956.

Mr. Rittenhouse: December 3, 1956, that is right.

Mr. Aronson: It was the date of the execution of the note and chattel mortgage.

Mr. Rittenhouse: That is correct; and this is in October.

The Court: Well, I will mark the appraisal at this time for identification and then I will listen to testimony as to whether or not the condition of the Los Gatos Lumber changed materially between October and December.

Q. (By Mr. Rittenhouse): Now, how was this particular appraisal made; do you recall?

A. Yes. [31]

Mr. Aronson: You mean the reason for it?

Mr. Rittenhouse: No—how.

Q. Did you observe how it was made?

A. Yes.

Mr. Aronson: May it be understood that I am objecting to the testimony with regard to the appraisal?

The Court: That is right.

The Witness: Do you want me to answer?

The Court: You may proceed.

Mr. Rittenhouse: Yes—How was it made?

(Testimony of Carl Morton.)

A. Mr. C. N. Uznay, who is an appraiser for the California Appraisal Company, came to our mill at our request. I authorized him to make an appraisal and he proceeded to do it, and stayed there, if my memory is correct, two or three full days and proceeded to inventory and check each piece of equipment of the physical assets of the mill—that was buildings and equipment.

Q. Now, with reference to the summary over here: Will you read that into the record; in other words, what is the summary or recapitulation of this appraisal?

A. Yes. Including all physical assets of the mill—the new replacement values, \$199,350.35; sound value, \$173,506.11; insurable value, \$160,900.25.

Q. Now, between the time that this appraisal was made and the date of the third day of December, 1956, were there any deletions or additions to the particular articles at the mill?

A. You mean physical assets? [32]

Q. Yes.

A. None to my knowledge, of any consequence.

Mr. Rittenhouse: Now with that, your Honor, I will offer this in evidence.

Mr. Aronson: Same objection—incompetent, irrelevant, and immaterial; self-serving for the purpose which I think is already established.

The Court: The testimony is that this appraisal was made by the California Appraisal Company; there is no objection with reference to this being a copy?

(Testimony of Carl Morton.)

Mr. Aronson: No. No objection to the fact that it is a copy.

The Court: And Mr. Morton has stated that in his opinion there were no substantial changes.

Mr. Morton: No.

The Court: The objection is overruled, and the document becomes Respondent's No. 3 in evidence.

Q. (By Mr. Rittenhouse): Now, with reference to the inventory value as recited in Trustee's Exhibit No. 1, which is dated July 31, 1956, will you read into the record the total of the current assets?

A. Yes. As indicated by the balance sheet dated July 31, 1956——

Q. Just the total.

A. The current asset figure is \$57,510.52.

Q. Now, with reference to Trustee's Exhibit No. 2, the current asset value is what on this, as of January 31, 1957?

A. The current asset value is \$13,253.37.

Q. Now, do you have any opinion as to what the value of the [33] assets as of December 3, 1956, would have been?

Mr. Aronson: I will object to that as calling for the opinion and conclusion of the witness. He might say "No."

Mr. Rittenhouse: I suggest you give him a chance——

The Witness: I would have to answer this way: We were in the process at that time of selling inventory——

(Testimony of Carl Morton.)

Mr. Aronson: I think that calls for a "yes" or "no" answer.

Mr. Rittenhouse: Do you have an opinion?

A. Yes.

Q. What is that opinion?

Mr. Aronson: I will make the objection that it is calling for his opinion.

The Court: Sustained.

Mr. Rittenhouse: I will call your attention to the pencil notations that are on this balance sheet dated 7-31-56, and your statement was, on direct examination, that they were your pencil notations; is that correct? A. Yes.

Q. Now when were they placed on this balance sheet? A. In August of 1956.

Q. And with reference to the words "into stock"; what does that mean?

A. At that time I was back in Colorado, talking to people and trying to get a loan for Los Gatos Lumber—I don't know the names of the individuals I talked to—and I was working with the balance sheet at that time to show that when stock was taken in lieu of notes payable to officers that the firm's balance sheet assumed a much better light and picture; if the [34] notes payable to officers were turned over into stock, were replaced with stock, that the firm would be in much better shape then, and I was talking to two men who might loan money to the corporation—we had agreed to do this—and the pencil notations were

(Testimony of Carl Morton.)

merely my working on that basis as to what would turn out.

Mr. Aronson: I move to strike all the last part of the testimony concerning the conversations and the reason for the pencil notations as being incompetent, irrelevant, and immaterial.

Mr. Rittenhouse: It shows the intention at the time these instruments were used and marked.

The Court: I think both you gentlemen and the Court will agree that the crux of this matter is that the money due these people was the difference between solvency and insolvency at the time of payment; that is the whole case as the Court sees it.

Q. (By Mr. Rittenhouse): Now, with reference to Mr. Gammill's advances: Was he aware of this understanding that you had with your family, that the notes would be turned into capital——

A. Into stock?

Q. Or into capital stock?

Q. (By Mr. Aronson): Upon a refinancing?

Mr. Rittenhouse: Upon a refinancing, yes.

Q. At that time, when Mr. Gammill advanced this money——

A. When he advanced it, yes.

Q. ——he was aware of this?

A. Yes, he was aware of it.

Q. And how many times did you discuss it with him? [35]

A. I don't remember the number of times.

Q. Was it more than once?

A. Yes, it was discussed some time back, and it

(Testimony of Carl Morton.)

was discussed with my former wife and myself in the spring. She was a note holder at the time.

The Court: We are concerned about the discussion with Gammill.

A. He was there at times; it was discussed prior to that time with George Stepovich.

The Court: All these times that Mr. Gammill was present?

A. I am talking of the times when he was present, and it was discussed with him. Of course that was when we were trying to get the Small Business Administration loan, and in the course of the statements and so forth it was discussed a number of times during the period of time, April on through until the refusal of the Small Business Administration loan.

Q. Well, now with reference to the particular advances of Mr. Gammill, when they were made the understanding that you had with your family was that your claims were to be subordinate to his particular advances; is that not correct?

A. Yes.

Q. And that understanding remained all during the time that he advanced it, during the time that this chattel mortgage was given; is that correct?

A. That is right.

Mr. Rittenhouse: For the purpose of the record, this Small Business Administration office is in San Francisco. I have secured certain photostats of certain portions of the record of the application, the original of which is in Washington.

(Testimony of Carl Morton.)

Q. Mr. Morton, I showed you these documents, or these [36] photostats? A. Yes.

Q. And you have examined them?

A. Yes.

Q. And what do they appear to be?

A. A copy of the original application.

Q. Of certain portions of it?

A. Certain portions of the application for a Small Business Administration loan.

Q. With particular reference to what was to be done with these applications to the members of your family? A. Yes.

Q. And these represented a true copy of the original that was filed with the Small Business Administration? A. Yes.

Q. Were the originals of these all signed by the parties involved? A. Yes.

Mr. Rittenhouse: I will offer this in evidence.

Mr. Aronson: I will object to that as incompetent, irrelevant, and immaterial.

The Court: Objection overruled. Respondent's No. 4 in evidence.

Q. Now, with reference to the letter from your mother and stepfather, marked Respondent's 2, for identification, was this authorization ever withdrawn or ever changed? A. No.

Q. As I understand—I will now offer this in evidence, your Honor.

Mr. Aronson: Same objection, your Honor. No. 2 in evidence.

(Testimony of Carl Morton.)

The Court: Overruled. Respondent's No. 2 for identification.

Q. Now, Mr. Morton, at the time of the alleged preference [37] given in December, your attorney at that time was whom?

A. George Stepovich.

Q. As a matter of fact, he still is your attorney?

A. Yes.

Q. Do you know who was representing Mr. Gammill? A. At that time?

Q. Yes. A. Bob Bennett—Mr. Bennett.

Q. Do you know who was representing Mr. Kelly at that time?

A. Mr. Rittenhouse—you.

Q. What was your understanding with reference to the demands of Mr. Rittenhouse? Were you going along with those, or what?

A. No. I objected to your demands. I objected to the demands of Mr. Rittenhouse at the time.

Q. (By Mr. Aronson): What objections?

A. For the chattel mortgage.

Q. What was the basis of your objection?

A. I didn't at that time want to encumber the Los Gatos Lumber Products with any additional indebtedness of the nature of a chattel mortgage when we were trying to get a loan from the Small Business Administration.

Q. How was this objection overcome?

A. By argument.

Q. That is a good answer. I show you a docu-

(Testimony of Carl Morton.)

ment dated March 15, 1957, and ask you whether or not you recognize the signatures here?

A. You just want me to identify the signatures now?

Q. Yes.

The Court: March of 1957?

Mr. Rittenhouse: Yes. This even shows the values at that time.

The Court: After the filing? [38]

Mr. Rittenhouse: Yes. The sole purpose of this is to show the fair value of the assets even after the filing of the petition; other than that I think it is incompetent, irrelevant, and immaterial.

Mr. Aronson: I agree with you. That document never came into being?

Mr. Rittenhouse: It is in being—here it is.

Redirect Examination

By Mr. Aronson:

Q. To clarify my mind, to make sure I understand it correctly, Mr. Morton, the question of the changing of the status of you and your family as far as the notes were concerned, or to change it to stock, was conditional upon the financing—obtaining of the financing? A. Right.

Q. As a matter of fact, if I remember your letter of the 10th—which is attached to Exhibit No. 4, says—the portion of the application of the Small Business Administration—that is exactly

(Testimony of Carl Morton.)

what it says—puts as a condition, “that said Los Gatos Lumber Products, Inc., obtains from Small Business Administration \$150,000.00 within 90 days from date hereof within the lifetime of Carl Morton.” That application had been made prior to the time these advances were made in October, November and December; is that right?

Mr. Rittenhouse: Portions, I believe, of the advances were made after December the third, and portions prior to December 3rd.

A. Yes. [39]

Q. Your letter of intent bears the jurat “Sworn and subscribed to before me this 10th day of September, 1956? A. Yes.

Q. And Mr. Gammill was fully aware of this application? A. Yes.

Mr. Aronson: I have nothing further.

Mr. Rittenhouse: Would you like to call Mr. Gammill, or should I?

PAUL GAMMILL, JR.

The Court: Mr. Paul Gammill has been previously sworn.

Cross-Examination

By Mr. Rittenhouse:

Q. You made an inquiry—I show you Trustee’s Exhibit No. 1 in this matter and ask you whether or not you have ever seen this before?

A. Yes, sir.

(Testimony of Paul Gammill, Jr.)

Q. Did you see it on or about the time it was made? A. Yes, sir.

Q. And did you at any time have conversations with Mr. Morton relative to this particular balance sheet and this statement? A. Yes.

Q. Where did they take place?

A. Well, this particular one took place at Mr. Morton's house. Mr. and Mrs. Morton and myself were discussing the idea or refinancing the loan.

Q. With reference to these particular items marked Notes Payable to Officers: What was the understanding or agreement relative to your advances and those particular parts of interest on the balance sheet? [40]

A. Well, my understanding was—we had an agreement with Mr. Morton relative to the fact that the notes were to be capital stock—they were to be replaced by stock.

Q. And was that at all times dependent upon the fact that it would be refinanced, or solely on the basis of your advances?

A. Well, that was on the basis of any advances; it was discussed with a number of people.

Q. What other people did you discuss it with?

A. You mean the people we discussed the transactions——

Q. Yes.

A. ——or people we discussed the finances with?

Q. No. When you were paying money into this company, who did you discuss it with?

(Testimony of Paul Gammill, Jr.)

A. We discussed it with Mrs. Kelly, Mrs. Sibly, Mr. Bennett; we discussed it with my father—it was just pretty near common knowledge—I mean——

Q. We are particularly interested in the discussions and your understanding at the time that you made these advances; in the discussions I want the members, if possible, who were present.

A. Well, we first discussed this way prior to my advances. In other words, Gammill's advances, and then there were discussions with Mr. George Stepovich.

Q. At this time was Mr. Morton present?

A. Yes. It was discussed about the refinancing at the time, and Mr. Stepovich brought up about the balance sheet himself. He was very upset at the assets and liabilities, and said, "We will have to do something here about the notes," and I [41] believe it was suggested by Mr. Stepovich and it was agreed by Mr. Morton that those notes would be cancelled and made into stock.

Q. Was that the date on which you advanced these funds and also the materials necessary for the operation of this mill?

A. Well, yes—without that I don't think anybody could operate.

Mr. Aronson: I ask the last part be stricken.

The Court: The last part will go out. That was the basis of your putting up of advances, for furnishing material.

A. Yes, I even discussed that with my family back home over the telephone. They wanted to

(Testimony of Paul Gammill, Jr.)

know the condition of the company, and I had mailed them a balance sheet and we discussed the balance sheet, and, of course, the first question they asked was about the notes, and that was discussed with Mrs. Kelly.

Q. Was that after it was changed?

A. No.

Q. First about the advances? A. No.

Q. And during this period of time why the chattel mortgage was executed and delivered; is that correct? A. Correct, sir.

Mr. Rittenhouse: I think I have no other questions.

Redirect Examination

By Mr. Aronson:

Q. You worked on the Small Business Administration with Mr. Morton, didn't you?

A. Yes, sir.

Q. And were fully aware of the contents of the application? A. Yes, I am—I mean——

Q. You were at the time it was presented, weren't you, Mr. [42] Gammill, you were familiar with the transaction?

A. I was familiar with the transaction, yes. I don't remember the content.

Q. But you had seen it at the time?

A. Right, sir.

Mr. Aronson: I think that is all.

Mr. Rittenhouse: The law requires four or five

different elements to establish what makes a preference.

The Court: Well, to avoid any misunderstanding we will submit it—20 and 15. The Trustee, to file the Opening Memo, will have 20 days, and the Respondent will have 15 days to reply, and the attorney for the Trustee to notify the Court as to whether or not he desires to file a Closing Memo, within 10 days; 20-15 and 10. Let the record show the Court has retained the six Exhibits.

[Endorsed]: Filed November 26, 1958, Referee.

[Endorsed]: Filed December 12, 1958, U.S.D.C.

[Title of District Court and Cause.]

CERTIFICATE OF CLERK
TO RECORD ON APPEAL

I, C. W. Calbreath, Clerk of the United States District Court for the Northern District of California, do hereby certify that the foregoing and accompanying documents and Exhibits are the originals filed in this Court and that they constitute the record on appeal as designated by the Attorneys for the appellant:

Petition by Creditors.

Statement of Affairs and Schedules.

Order of Reference.

Order of Adjudication.

Order to Show Cause.

Trustee's Objection to the Proof of Secured Claim of Emmet L. Rittenhouse.

Findings of Fact and Conclusions of Law.

Order Allowing Secured Claim.

Referee's Certificate on Petition of Findings of Fact and Conclusions of Law and Order Allowing Secured Claim.

Notice of Hearing.

Order Affirming Referee.

Notice of Appeal.

Designation of Contents Record.

Transcript of Hearing on Order to Show Cause.

Trustee's Exhibits 1 and 2.

Respondents Exhibits 1, 2, 3 and 4.

In Witness Whereof, I have hereunto set my hand and affixed the seal of said District Court this 13th day of January, 1959.

[Seal]

C. W. CALBREATH,
Clerk;

/s/ WM. J. FLINN,
Deputy Clerk.

[Endorsed]: No. 16330. United States Court of Appeals for the Ninth Circuit. Charles E. Hoppe, Trustee of the Estate of Los Gatos Lumber Products, Inc., Bankrupt, Appellant, vs. Emmet L. Rittenhouse, Appellee. Transcript of Record. Appeal From the United States District Court for the Northern District of California, Southern Division.

Filed: January 13, 1959.

Docketed: January 22, 1959.

/s/ PAUL P. O'BRIEN,

Clerk of the United States Court of Appeals for the Ninth Circuit.

United States Court of Appeals
for the Ninth Circuit

No. 16330

CHARLES E. HOPPE, Trustee of the Estate of
Los Gatos Lumber Products, Inc., a California
Corporation, Bankrupt,

Appellant,

vs.

EMMET L. RITTENHOUSE,

Appellee.

APPELLANT'S CONCISE STATEMENT OF
POINTS URGED ON APPEAL

Comes now Charles E. Hoppe, Trustee, Appellant herein, and in accordance with Rule 17(6) of the Rules and Practice of the United States Court of Appeals for the Ninth Circuit, specifies the following as a concise statement of the points on which he intends to rely on this appeal from the Order made and entered by Honorable Oliver J. Carter, Judge of the United States District Court for the Northern District of California, on the 19th day of December, 1958, more particularly specified and described in the Notice of Appeal heretofore filed with the Clerk of said District Court on the 31st day of December, 1958, as follows:

1. That said Order was not supported by the evidence and is contrary to the law in that:

(a) The District Court in said Order erred in finding that the Findings of the Referee in Bankruptcy were not "clearly erroneous."

(b) The District Court in said Order erred in holding that the Findings of Fact 4, 5, 6 and 7, and each of them, were supported by the evidence adduced upon the trial of the issues.

(c) The District Court in said Order erred in sustaining the Order of the Referee in Bankruptcy that the chattel mortgage, which is the subject of controversy herein, was not a preferential transfer within the meaning of Section 60 of the Bankruptcy Act.

Dated this 22nd day of January, 1959.

SHAPRO & ROTHSCHILD,

By /s/ DANIEL ARONSON, JR.,
Attorneys for Charles E. Hoppe, Trustee of the
Estate of Los Gatos Lumber Products, Inc., a
California Corporation, Bankrupt.

[Endorsed]: Filed January 20, 1959.

